



State Investment Commission
Monthly Meeting Minutes
Wednesday, March 26, 2014
9:00 a.m.
Room 205, State House

The Monthly Meeting of the State Investment Commission (SIC) was called to order at 9:08 a.m., Wednesday, March 26, 2014 in Room 205, State House.

I. Roll Call of Members

The following members were present: Mr. J. Michael Costello, Mr. Thomas Fay, Mr. Robert Giudici, Mr. Thomas Mullaney, Ms. Marcia Reback, Mr. Andrew Reilly, Mr. Frank Karpinski, and General Treasurer Gina Raimondo.

Also in attendance: Mr. Thomas Lynch of Cliffwater, alternative investment consultant to the Commission; Ms. Katherine Dowling of Thoma Bravo; Mr. John Burns of Pension Consulting Alliance (PCA), general consultant; Ms. Sally Dowling of Adler Pollock & Sheehan P.C., legal counsel; Ms. Faith Lasalle, Esq., Chairperson of the Rhode Island Higher Education Assistance Authority (RIHEAA) Board of Directors; Mr. Seth Magaziner, candidate for treasurer; Ms. Anne-Marie Fink, chief investment officer, and members of the Treasurer's staff. Treasurer Raimondo called the meeting to order at 9:08 a.m.

Ms. Paula McNamara was absent.

II. Approval of Minutes

On a motion by Mr. Mullaney and seconded by Mr. Costello, it was unanimously

VOTED: to approve the draft of the minutes of the February 26, 2014 meeting of the State Investment Commission.

III. Private Equity Recommendation—Thoma Bravo XI

Mr. Lynch introduced Thoma Bravo, a private equity fund Cliffwater recommends for the portfolio.

Ms. Katherine Dowling gave an overview of the firm. She said Thoma Bravo has a long history in middle-market private equity. She noted the team has deep sector knowledge in the software industry. They've had close to one hundred software firm purchases in the last several years. Their strategy is to maintain a watch list of the companies in the industry and maintain contact with them.

They strive to be the go-to entity when companies want to make a move. This approach enables them to get access to proprietary deals when something is happening. They look for companies that have recurring revenue of at least 50%. During the diligence time and even prior to it, they have already identified possible add-on acquisitions and efficiencies. In this way they can move quickly to make offers and close deals.

Ms. Katherine Dowling said Fund XI would have \$3.4 billion in limited partner commitments with the general partner commitment in addition. She reviewed their team and the work personnel do on strategy.

The board asked questions and Ms. Katherine Dowling left the room.

Mr. Lynch added that software is a big component of the economy today and Cliffwater finds this sector appealing. Secondly, Cliffwater looks for firms which have more advantage in getting

investment transactions and that can add a lot of value to the companies they acquire. He added that Thoma Bravo has a very experienced team and their performance has been outstanding. Treasurer Raimondo asked if Cliffwater has any other clients going into the fund and if they would represent enough of the investor base to push back on the fees.

Mr. Lynch said they have been trying and they will continue to try. He noted that many of their pension fund clients would still commit to the fund with the firm's higher-than-market fee because the performance has been so good.

Treasurer Raimondo expressed concern over the lack of a hurdle rate in the fund.

Mr. Reilly echoed the Treasurer's concern and also expressed concern over the velocity of capital and the fees.

The board discussed the recommendation. They asked Mr. Lynch to communicate their concerns to the firm in hopes of negotiating more attractive terms. No vote was taken.

IV. Private Equity Quarterly Review

Mr. Lynch presented the calendar year-end private equity review. He noted final numbers as of year-end weren't available for all the partnerships. Last year there was a record amount of distributions. High levels of IPOs, sales of companies and dividend recaps led to strong flows of capital from partnerships back to limited partners. In terms of outlook, Cliffwater isn't currently green-lighting any private equity category because valuations are high. Their preference within the buyout category continues to be firms that focus on smaller transactions and sector-specific funds.

He reviewed the portfolio. He noted that the portfolio has exceeded the amount of capital invested and produced very good long-term rates of return. He reviewed the flow of capital for calendar year 2013. The portfolio had net gains of \$73 million for the year. Distributions exceeded contributions 3 to 1. The return for the year was 13.8% so performance continues to be strong.

Mr. Lynch reviewed the drivers of performance and noted that there were a lot of positive drivers. The few disappointments were in venture capital. He reviewed top long-term performers and noted that they continue to be some of the commitments made in the most recent years.

Mr. Lynch added that the portfolio has good diversification.

Mr. Costello asked about the number of limited partnerships and Mr. Lynch said they were looking to decrease the number of manager relationships, not necessarily the number of funds.

Mr. Costello expressed a preference that the committee focus on diversifying vintage years in a methodical way and not put as much importance on hitting the 7% private equity allocation quickly. Mr. Lynch agreed and said historically, when distributions exceed contributions, one may want to slow down commitments.

The board asked more questions.

Concerning the hedge fund portfolio, Mr. Lynch informed the SIC that Indus Asia Pacific fund has been put on Cliffwater's watch list. He cited concerns about modifications in concentration and the roles of the portfolio managers, but noted that the concerns were not yet at a level where Cliffwater would recommend redemption. He also noted that the fund has not performed as well as expected as Asian markets have been particularly challenging. Because of their performance Indus has made a moderate portfolio strategy change to be more concentrated with their positions. In addition, they have switched from two co-portfolio managers to one sole manager. This portfolio manager has also relocated from Hong Kong, where most of their research is being done, to Indus's San Francisco office.

V. Legal Counsel Report—Securities Litigation Discussion

A motion was made by Mr. Reilly and seconded by Ms. Reback to convene into executive session pursuant to Rhode Island General Law §42-46-5 (a) (2). A roll call vote was taken to enter executive session and the following members were present and voted Yea: Mr. J. Michael Costello, Mr. Thomas Fay, Mr. Robert Giudici, Mr. Thomas Mullaney, Ms. Marcia Reback, Mr. Andrew Reilly, and General Treasurer Gina Raimondo.

It was then unanimously

VOTED: To convene into executive session pursuant to Rhode Island General Law §42-46-5 (a) (2).

It was reported to the public that three votes were taken during the executive session. In the first vote, it was unanimously voted to join the existing lawsuit against The Royal Bank of Scotland (RBS) regarding RBS's rights issuance of April 30, 2008 and to seek all recourse with the assistance of Grant & Eisenhofer. The second vote taken during executive session was a unanimous roll call vote to seal the minutes of the executive session of March 26, 2014 and a third to exit the executive session.

VI. CIO Report

Ms. Fink reviewed the performance for the month of February. The portfolio was up 2.9% which puts it at 11% fiscal-year-to-date. Risk and return continue to be better than the bottom-up benchmark and the basic 60/40 plan so the asset allocation is working. She reviewed the overall investment environment for the month. The equity hedge fund portfolio benefited from increasing focus on fundamentals and dispersion among stocks. The strong environment also helped the private equity funds. The absolute return hedge funds were up about 1%, which is slightly less than the benchmark due to their lower equity sensitivity and the strong equity markets. Real estate and GILBs were in line with their benchmarks and were solid performers. Ms. Fink noted that the bank loan portfolio was a bit disappointing in February, particularly PIMCO which staff will continue to monitor.

Ms. Fink gave a brief update on the *CollegeBoundfund*. She said the options approved by the committee have gone into effect and are now available to participants. She added that the RFP for a consultant has been expanded to include additional elements.

Ms. Fink gave an update on the Third Point redemption and said it will be effective as of March 31st.

VII. Treasurer Report

Treasurer Raimondo gave a brief update on a recent meeting with AllianceBernstein regarding the *CollegeBoundfund*.

She thanked the board and commended them on their continued work.

There being no other business to come before the Board, on a motion by Ms. Reback and seconded by Mr. Fay the meeting adjourned at 10:56 a.m.

Respectfully submitted,

Gina M. Raimondo
General Treasurer